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Reflections on Expropriation and the Future of Investment in the Americas

This writer's experience in the private area of investment in developing countries derives from three distinct periods and roles—first in private practice, then in United States government service, and then in academic life. Whether these varieties of legal experiences add up to a coherent whole is questionable. But looking at the problem from three different angles over time may provide some viewpoints not apparent to those with a more constant perspective.

I

In private practice in the late 1950s, one of the recurring tasks of international lawyers was to try to search for ways to increase security of investments in less developed countries (to use the euphemism of that decade), and to try to come up with disincentives for large-scale expropriations. It is not clear how one should evaluate the result of those endeavors—certainly nothing that any private lawyer did in New York or London or Paris or Amsterdam deterred a Sukarno or a Castro. On the other hand, those years did see the beginning of a gradual realignment in the perception of the relations between alien investors and host countries. The position of investors in foreign countries was seen somewhat less in terms of property rights—eternal and immutable—and more in terms of a continuously changing contractual relationship, in some ways like a collective bargaining agreement.

II

In the Legal Adviser's office of the United States State Department in the early 1960s, there were three missions concerned with foreign investment in Latin America—(1) encouraging new investments, (2) defend-

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ing existing investments, and (3) protecting United States policy from the consequences of investment disputes. The conflict among these three missions is not generally appreciated—certainly was not appreciated at the time.

This was the period not just of Camelot, but of genuine optimism, and genuine dedication to the cause of bettering the economic standards of what were now called 'the developing countries'. It was a mixture, of course, of generosity and self-interest. But the New Frontier, from the President down, believed that misery bred revolution, whereas economic growth, political democracy, and social justice would reinforce one another in the march toward attainment of our common ideals.

How could economic growth be achieved? The figures were less encouraging than the slogans. However one counted—whether in terms of the movement of prices of primary products compared with prices of necessary imports, or in terms of income or GNP per capita, or the overall share of the world's capital, the developing countries' outlook was gloomy. But try we must, sustained perhaps by the analogy of the postwar recovery of Europe. At Punta del Este in August of 1961, the countries of the Western Hemisphere were led by the United States to pledge themselves to a rate of economic growth for each country in Latin America of not less than 2.5 per cent per capita per year.[1]

No one quite knew what this minimum goal would require in the way of transfer of resources from the developed countries, but by any count the sum was enormous—somewhere between \$5 and \$20 billion per year. Whatever the precise amount, it was clear that no foreign aid program depending solely on public funds, whether by the United States alone, by the international community in whatever manner mobilized, or by some combination of national and multinational effort, was likely to sustain a resource transfer of that order of magnitude over a decade.[2]

The answer? In the minds of United States policy-makers—private investment. And this answer was doubly attractive, in that private investment could accomplish not only a transfer of capital, but could, at the same time, accomplish a transfer of technology and know-how, and also provide export markets. By putting the equation this way:

$$\text{Need} - \text{public funds} = \text{private investment};$$

[1]Charter of Punta del Este Establishing an Alliance for Progress within the Framework of Operation Pan America. 45 DEPT. OF STATE BULL. 463 (1961).

[2]*See, e.g.*, Agency for International Development, *Foreign Aid through Private Initiative*, REPORT OF THE ADVISORY COMMITTEE ON PRIVATE ENTERPRISE IN FOREIGN AID (the Watson Committee) at 2 (1965).

it is not intended to suggest that the designers of our aid policy in the early sixties were wholly naive. They worried about "investment climate" and they designed a variety of protective mantles against the disagreeable winds blowing from the south. They developed the investment guarantee program, for instance; they supported local partnerships; and they promoted the use of intermediaries, such as IFC or local development banks.

The idea of private investment as the device to fill the resource gap not only did not work, but led to a continuing and self-reinforcing series of misunderstandings. For one thing, business was likely to go where the greatest hope for profit lay—or at least the most favorable combination of high profit and low risk. That, after all, is the business of business. But there was no reasonable expectation that investment made on this calculation would go to countries with the greatest need, or (in those countries where it did go) to the industries with the greatest promises of developing the local economy.

But even leaving that point aside, the coupling of private foreign investment in developing countries with the explicit foreign aid goals of United States policy did not ring true, just when economic ambition and nationalism were rising up in nearly all the developing countries. Foreign investment had been going on in Latin America for several generations, with no particular identification with United States government purposes. The benefits to host countries, while in some cases considerable, seemed to have been by-products rather than principal goals, and in any event were seen as equivocal.

Looking back now from the vantage point of the 1970s, the confusion of motives seems inevitable. (1) Private investment was seen as hypocritical in its latter-day pose as an instrument of economic betterment of the host country; and (2) the aid-giving countries—particularly the United States—were accused of being interested primarily in protecting their nationals' private investments and only secondarily in economic development. Both points were often reinforced by the inconsistent responses to the dilemma facing any aid program—whether to support established institutions or to try to replace them.

Inevitably, then, the issue of encouraging new investments blended into the problem of protecting existing investments—the second of the three missions mentioned above. Whenever—or at least so it seemed—an investor was threatened with a take-over or was denied a license to do something he had been doing, or was subjected to new and burdensome taxes, he or his counsel would come to the State Department for support. Sometimes the approach was made to the regional bureau or assistant secretary, sometimes to the Bureau of Economic Affairs, sometimes to

AID, and sometimes to the seventh floor. Eventually, however, most situations of this kind involved some type of contractual or statutory claim, and more likely than not they landed in the Legal Adviser's office.

How should an American government lawyer deal with such a situation? One way might be to say: "We deal only with international law violations; an international law violation occurs when you have exhausted your local remedies; and until you have done this, just keep us on your mailing list." A variation of that attitude might be to say, (where applicable) that the investor has given up his right to protection of his home country—either by incorporating in the country of investment, or by signing a contract with a provision undertaking to forego all diplomatic protection by his own government (the so-called Calvo Clause), or by investing in a country which has a form of the Calvo Clause as part of its law or constitution. But any response along these lines, at least at the first stage, is out of the question today for any government reasonably responsive and responsible to its citizens. Quite apart from scholastic arguments about the validity of the Calvo Clause—whether for instance a citizen can ever waive the right of his government to present a claim—the Calvo doctrine or the exhaustion-of-remedies doctrine are without practical meaning. When an investor looks to his government for help in circumstances such as those described, the first disposition of his government will be to do what it can. Not only will the investor's government not decline to do what it can for its citizens—within limits, of course; the host government will not in the author's experience raise technical arguments along the above lines if the investor's government begins to take an interest in the dispute.

What, then, can the investor's government—typically the United States—do in such a situation? Various pressures can be brought to bear—aid, commodity agreements, political arrangements, and so on. Where a dispute is about money, intervention on the part of the investor's government, if done quietly, may play a decisive role. For the lawyer—whether private or in government—an important role is to try to do the opposite of what we learned in law school—that is not to look for the principle to be derived from a particular dispute, but to look for a particular issue that can be compromised, renegotiated or paid for without either agreement on or compromise of principle.

Of course, when the dispute is really one of principle, there is little the government can do—with or without a lawyer. The contrast between the situation of the copper companies in Chile in the mid-1960s and today illustrates the point. When President Frei was elected on the platform of Chileanization, it proved possible to work out an arrangement to preserve everyone's position of principle, and at the same time—by no means incidentally—to strengthen United States foreign policy in Chile. Used in an affirmative way, our foreign aid tools, including Ex-Im credits and investment guarantees, both protected a major investment by United States-based enterprises and promoted the foreign policy interests of the United States—seen at that time as supporting left-of-center Christian democracy throughout Latin America. In this writer's view, contrary to what has been written by some of the revisionist critics of United States policy, the foreign policy goal was probably more important than the protection of an existing investment in persuading the United States government to become the third partner in the Chileanization program. When the conflicts of principle became irreconcilable, however, as happened after 1970, there seemed to be no further use in looking for details, such as trying to convert equity to debt or establishing joint venture operations, or arranging management contracts or whatever. And certainly negative use of foreign aid—whether or not justified on other counts—is going to have no value in protecting the investment or changing the host country's mind.

This brings us to the third of the missions in this area as a government official—the preservation of foreign policy interests of the United States from the effects of investment disputes. It is hardly necessary, in this audience of professionals, to talk at length about the Hickenlooper Amendment.[3] Only two brief points need be made here: (1) Even the Hickenlooper Amendment did not say "Aid will be cut off for any country that expropriates. . . ." What it said—that is what could muster a majority in the Congress—was "aid will be cut off for any country that expropriates and has not within 6 months of such action taken appropriate steps to discharge its obligations under international law." The mandatory character of the amendment, in contrast to most of the other restrictions on aid which could be waived by the President,[4] meant that every dispute over an investment, however small—and some of them were indeed small—potentially involved an important tool for conducting the foreign policy of the United States. Indeed, as suggested in the preceeding discussion, an investment dispute with a country might well prejudice measures taken in connection with other, more important investment disputes. Just as juries in England would acquit thieves rather than send them to the gallows, so the Hickenlooper Amendment induced on the part of the United States government lawyers great caution about ever speaking out, ever taking sides in investment disputes. They found, as many of you know, a variety of ways of in-

[3]§ 620(e) of the Foreign Assistance Act of 1961, *as amended*, 22 U.S.C. 2370(e) (1970).

[4]*See, e.g.*, § 620(a)(b)(c)(d)(f)(j)(p)(q). The non-waiver provision of the Hickenlooper Amendment was subsequently incorporated into some of the other provisions— *e.g.* § 620(g)(i)(k); for the general waiver authority, see § 614(a).

terpreting the words "appropriate steps," or "obligation under international law." After a while, as one of the author's colleagues is fond of saying about faculty meetings, there were lots of cases but no law.

III

The author left the State Department in 1966, before the recent changes in direction in Peru and Chile, and for the past six years he has been thinking about the problem of private investment in developing countries from the luxury of a professor's chair. In a way, that has turned out to be the most difficult assignment, because there was neither a client nor a boss nor any categorical imperative to serve as a guide. One may believe (as this writer does) in economic development, and (at least for the countries that he knows something about) in private enterprise. One may also continue to believe in foreign aid, though perhaps not with the confidence and optimism of a decade ago. But at least to this observer, there is a good deal of doubt about President Nixon's statement, as part of his updating of the Hickenlooper principle early this year, that "a sort of symbiosis exists—with government aid efforts not only speeding the flow of, but actually depending for their success upon, private capital, both domestic and foreign."[5]

President Nixon may be right when he says that actions impairing the contractual rights or seizing the assets of foreign investors are "wasteful from a resource standpoint." He may even be right, simply in terms of the priorities that he sees for the United States today, that foreign aid does not seem so attractive in the face of expropriations and similar acts. It does not follow, however, that the conditions for private investments of the kind he advocates exist today in the Western Hemisphere.[6]

Whether one is content to recite principles of international law developed in an earlier age, or like President Nixon, one says to the developing countries, in effect, "I know what is good for you," the result seems to be about the same. We cannot change the receptivity of the hemisphere to private investment by cost-benefit analysis. One would hope however that doubt about conditions for private investment would not erode the willingness of developed countries to dedicate a portion of their resources to public assistance of some sort—whether bilateral or multilateral.

There may be some small contributions that we can make as lawyers. We may, for example, try to separate the question of public v. private

[5]Policy Statement on Economic Assistance and Investment Security in Developing Countries, Jan. 19, 1972, 8 WEEKLY COMP. PRES. DOCS. 64 (1972).

[6]*Compare, e.g.*, Schliesser, *Recent Developments in Latin-American Foreign Investment Laws* 6 INT'L LAWYER 64 (1972).

ownership from the question of national v. alien ownership. This is, in a sense, what Mexico has done. It is only fair to point out, however, that Mexicanization as understood today is taking place a full generation (or, depending on one's definition, two generations) following the revolution in that country. Whether, as has been suggested, international financial institutions should take up this idea—for example by financing the purchase by local nationals of enterprises owned from abroad—may be worth thinking about. Speaking from the stacks of the library, all this writer can do is to summarize briefly the results of the study undertaken by the Inter-American Law Center of Columbia University which focused expressly on expropriation within the countries covered, rather than on transnational issues.[7]

It turns out that even excluding entirely the problem of alien ownership, in an age of social change, discontent, and rejection of old values, the classical view of property embodied in the civil codes of nineteenth century Europe and Latin America, no longer holds up—at least in the big cases. When the traditional doctrines get in the way of political movements—left or right, violent or peaceful—they tend one way or another to be cast aside. Whether there is a constitutional amendment or a special agrarian law, or a technique of valuation known to be unrealistic, or a re-definition of 'cash payment'—the relation of the state to private property developed when property was supreme and the state was modest, does not survive the recasting of the state as the principal focus of values.

Property, in nearly all the countries we looked at, is said to have a "social function." The definition of that term is, as one might expect, not clear. It is clear, however, that to call transfer of major industries from private to public ownership illegal, is to rely on a law that is no longer firm. The foreign investor is a special case—in some ways more vulnerable, in others more protected. But nowhere in the developing countries—at least in Latin America—is there, in this writer's judgment, the security of investment that can support long-term economic growth through private capital.

This is not to suggest that there are no more reasonable investment opportunities in Latin America. But it seems probably that future investments in Latin America will be either the kind that is designed to be in and out within five years, or the kind that relies for its profits on activities outside the host countries—so called downstream profits. And the more investment that takes this form, the more support is likely to arise for those

[7] EXPROPRIATION IN THE AMERICAS, A COMPARATIVE LAW STUDY Andreas F. Lowenfeld, editor. (Dunellen, New York, 1971).

who will say "we told you so" in their attacks on capitalism and foreign exploitation.

It may be that the pendulum will swing the other way, as seems to be the case in Brazil today. But as long as the pendulum is swinging, the prospects seem dim for stable long-term investments that create both useful economic activity for the receiving country and an adequate rate of return for the investor. Only when the pendulum stops swinging, as is perhaps the case in Mexico today, will we be able to make a realistic assessment of the role of private enterprise in the future of the hemisphere.